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DEPARTMENT OF STATE
THE DIRECTOR OF INTELLIGENCE AND RESEARCH

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Mexico -
LAPC 6/14

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TO : ARA - Mr. Martin, Chairman
Latin American Policy Committee
FROM : INR - Roger Hillsman *Rog Hillsman*
SUBJECT: Mexico and the Alliance for Progress

The following study on Mexico has been prepared in connection with the meeting of the Latin American Policy Committee to be held June 14.

Background

The Mexican Revolution of 1910 broke down old barriers of caste and race and gave the government an important role as provider of basic economic and social services. The government has also long functioned as arbiter between labor and capital, giving benefits to each group as needed to assure political stability. Important commercial and industrial groups, commercial farmers in the northern states, and much of urban labor, especially privileged union groups such as the petroleum workers, have been fundamentally satisfied with moderate course pursued by the government in recent decades. Becoming increasingly restive are those groups which have not benefited economically from the revolution. These include particularly the communal farmers and peasants of the central plateau area where the pressure of burgeoning population on small, uneconomic plots of land is reducing levels of living, breeding unrest, and leading to troublesome urbanization of unskilled labor.

Political situation

Mexico is ruled by the Institutional Revolutionary Party (PRI), which maintains virtually absolute control over the political life of the country

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the country. Nearly 40 years in office, the PRI governs in the name of the continuing Mexican Revolution and is the only channel through which political advancement can be obtained. The party embraces heterogeneous groups of political elements ranging from the extreme left to the conservative right and has had remarkable success in accommodating and reconciling the divergent interests and ambitions of its members. President López Mateos, in keeping with his own views, has followed a left-of-center course on occasion radical enough to satisfy even the extreme left, but has stopped short of actions which would alienate the more conservative elements within the PRI.

The political climate became openly unsettled during 1961 when left-wing extremists, including some elements within the government party, PRI, made a bold effort to increase their influence, claiming that Castro-like policies were necessary to halt what they depicted as a drift from the original aims of the Mexican Revolution. A large role was played by left-leaning former President Cárdenas, who still commands the affection and loyalty of numbers of Mexicans, especially among the peasants and small communal farmers (ejidatarios). Despite his leftist leanings, however, Cárdenas has remained within the PRI.

The intensification of leftwing activities shook the business community and other moderate elements, which responded with vigorous anti-Communist campaign. Partly as a result of this campaign and of the gradual decline of Castro's appeal throughout the hemisphere, middle-of-the-road Mexicans seemingly have regained the political initiative. Jockeying preliminary to presidential elections in July 1964 has already begun.

Communism

Mexico has long been a major center for the international Communist movement in Latin America. Mexican sympathies for the social revolutionary aspects of the Cuban revolution, historic opposition to intervention, and suspicion of the US fostered by historic relations, have provided an atmosphere from which the communist movement has profited recently. Estimated membership in a miniscule Trotskyite party (POCM), the 3,000-member orthodox Mexican Communist Party (PCM), and a much larger Marxist party (PPS) totals somewhat under 50,000. The PCM exercises strong influence in the Movement of National Liberation (MLN), a rabidly anti-US, pro-Cuban mass organization established in 1961 under the leadership of leftist ex-President Cárdenas. The Mexican Government continues to tolerate extreme leftists in the Foreign Ministry and other departments

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and in the educational system. Communists are also prominent in some peasant groups and a few labor unions. The large student federation at the National University, and its affiliated schools is not Communist-directed, but is given to irresponsibility and has on occasion been effectively manipulated by its strong Communist minority.

Economic situation

Economic solutions are not readily available for the problem of the increasingly discontented rural and slum-dwelling masses. It is now obvious that neglect of Mexico's human resources is posing both economic and political threats to the industrial and commercial elite. The population is increasing by about 1 million persons or 3.1% annually, bringing roughly 350,000 people into the labor force each year. The cheapness of labor and its low productivity constitute increasing major deterrents to improving levels of living. Nevertheless, Mexico is not without assets in coping with the problems of an unfinished revolution and the stresses of economic development.

Mexican economic development has been considerable since 1940 when industrialization began in earnest. Since then, the physical output of goods has more than doubled with average real growth in excess of 6% a year through 1956. From 1957 to 1960 the annual growth rate slowed down to an average of 5% dropping to 3.5% in 1961 and adding only a little to per capita income in the face of a population increase estimated at 3.1% per annum. Nevertheless, per capita income has risen considerably for the period as a whole and now is equivalent to US\$320. Furthermore, Mexican output has acquired a composition characteristic of a reasonably advanced economy. Industry (manufacturing, construction, petroleum and electric power) accounts for over 35% of GNP, considerably more than agriculture with 20%. And even in agriculture a large part of the output is from commercial rather than subsistence farming. Mexican exports are more diversified than those of any other Latin American country, and only 20% of imports are consumer goods.

The public sector of the economy -- when measured in terms of its direct contribution to the GNP -- seems to occupy a minor role. To be sure, the government owns the petroleum industry, the electric power industry and the railroads; some major steel plants, fertilizer plants, railroad equipment plants and various lesser industrial establishments; a number of commercial and industrial banks; organizations engaged in the distribution of foodstuffs and newsprint; and a variety of other

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institutions. Still, the activities of these enterprises plus those of the governmental institutions proper account for little more than one-tenth of GNP. The total tax burden in Mexico is among the lowest in the world -- around 11% of GNP. Limited revenues, which from 1957-1960 failed to grow as fast as real GNP, have meant substantial federal deficits in recent years as the government has rapidly increased capital expenditures and spending for social services while paying out subsidies to state enterprises, particularly the railways, petroleum and electric power entities. Aware of its need to improve its financial position the administration has introduced a limited income tax reform, which will increase revenue from that source to some extent and has lately indicated that it may move to reduce subsidization and limit access to central banking financing of deficits.

The government's role in capital formation is far larger than its contribution to GNP, currently accounting for around 40% of total investment. This proportion is rather low by Latin American standards although it has been increasing since 1957 as a result of expanded government outlays in the face of a slight decline in private investment as a percentage of real GNP. Since 1956 approximately 80% of government investment has gone into irrigation, electric power, petroleum and transportation with most of the balance going to social investment in public health, housing, education and research.

During the period 1962-64 most government investment is scheduled to increase in absolute terms with irrigation and social investment intended to increase most sharply over 1961 levels. In the absence of new taxes or reduction of subsidies, ambitious increases in government spending will require extremely large-scale internal or external financing.

The private sector of the Mexican economy has been one of the most dynamic in Latin America. It has successfully installed a full range of consumers' goods industries and many producers' goods plants, developed commercial agriculture for the local and export markets, and improved marketing and distribution systems.

The slowdowns in the rate of private capital formation and in the overall rate of growth in the period since 1957 are of obvious concern. There is no precise explanation of the trend but many factors have been mentioned and they have doubtless had a cumulative, negative effect. Among them are the sluggishness of the US economy, which has a depressing

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economic and psychological effect on Mexican business; the lower world prices obtaining for exports of coffee, cotton, and Mexican minerals; a lessening of easy opportunities for small investments yielding high returns; limitations placed on the internal market by inequitable distribution of income; and the limited availability of credit for the private sector in recent years. In addition, private loss of confidence stems from the fears of domestic capital regarding government intervention in business, apprehensions of foreign capital concerning the Mexicanization of enterprises, fears of radical social reforms and fears of Castro-communism. Such fears brought on a serious capital flight in 1961.

Economic prospects

Improvement in economic conditions in the United States would provide a much-needed shoring up of the confidence of the ruling bourgeoisie and induce them to renew their previously vigorous entrepreneurial operations. Mexico, more than any other Latin American country, is locked into the US economy on which it depends in myriad ways -- as its chief market, source of tourist receipts, outlet for surplus labor, supplier of foreign investment and technology and, to an important extent, a moulder of businessmen's attitudes. The direction of Mexico's GNP curve since 1940 has closely paralleled that of the United States and there is a strong likelihood that if the US economy pulls ahead Mexico will again achieve satisfactory growth rates.

In terms of its own resources and efforts, there are a number of steps that Mexico can take to encourage development. A step-up in gross domestic investment might be accomplished by reducing the threat of government competition with private enterprise. At the same time a fiscal policy that helps to redistribute income somewhat and increase demand for local manufactures and services could stimulate business. Correction of the urban-rural imbalance cannot be quickly realized but gradual improvement could be achieved with additional rural credit to small as well as large farmers and by transplanting of excess population from the central plateau to newly developing regions in the south-central area. Vocational education for the more restless, urbanizing elements of the rural population would also facilitate transfer into urban occupations.

Alliance for Progress prospects

Mexico is likely to be only a limited partner in the Alliance for Progress. The country's strong nationalism is expected to limit its willingness

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to advertise cooperation with the United States' assistance programs. A government investment plan has been submitted to the OAS and the IBRD and a program of frontier development designed to renovate border towns along the Rio Grande has been announced. Officials and financial experts continue to resist planning for development on a national basis, preferring to draft plans by sector, such as railroads, power, irrigation or a specific industrial development. It seems probable that Mexico will continue to rely on IBRD and Ex-Im bank loans for external financing of major economic overhead projects.

Mexico's interest in foreign aid for social overhead projects will be shaped by domestic political decisions. Depending on the exigencies of the moment, Mexico may seek loans for rural credit, colonization and possibly housing. The country's nationalistic views regarding education will probably limit its interest in foreign assistance in this field.

If the commercial and industrial interests that have guided policy for nearly two decades continue to dominate the political situation, it seems probable that they will not encourage projects that build up government economic operations. They view government as a useful partner for private capital and as a buffer against large-scale popular demands. They do not wish to see a build up of new privileged sectors of the population although they would probably permit limited assistance to the masses if it reduced politically dangerous unrest.

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